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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

June 30, 2005

MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

June 30, 2005

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APPOINTIVE OFFICIALS

George Parisot, Lottery Director

John Tarr, Lottery Assistant Director for Security

LOTTERY COMMISSION

TERM EXPIRES

Tom Keegan	Helena	January 1, 2006
Betty Wilkins	Missoula	January 1, 2006
Robert Crippen	Butte	January 1, 2007
Wilbur Rehmann	Helena	January 1, 2009
Craig Anderson	Glendive	January 1, 2009

REPORT DISTRIBUTION

According to Section 23-7-202(9), MCA, copies of this report must be distributed to the following:

Governor – Brian Schweitzer
Director of Dept. of Administration – Janet Kelly
Legislative Auditor - Scott Seacat
President of the Senate – Jon Tester
Speaker of the House – Gary Matthews

The law also states "the President of the Senate and the Speaker of the House will determine the report distribution to each member of the appropriate committee of each house of the legislature". The President of the Senate and the Speaker of the House have requested that this report be distributed to the following committees:

HOUSE – State Administration Committee

Larry Jent, Chair	
Dee Brown, Vice Chair Majority	
Veronica Small-Eastman, Vice Chair Minority	
Joan Andersen	
Mary Caferro	Hal Jacobson
Sue Dickenson	William Jones
Emelie Eaton	Gary MacLaren
Robin Hamilton	Bruce Malcolm
Gordon Hendrick	Alan Olson
Teresa Henry	Bernie Olson

HOUSE – Business & Labor Committee

Jim Keane, Chair	Llew Jones
Kathleen Galvin-Halcro, Vice Chair Majority	Mike Jopek
Joe McKenney, Vice Chair Minority	Harry Klock
Elsie Arntzen	Scott Mendenhall
Bob Bergren	Mike Milburn
Tim Dowell	Don Roberts
Kevin Furey	Wayne Stahl
Dave Gallik	Dan Villa
Ralph Heinert	Jonathan Windy Boy

SENATE – State Administration Committee

Carolyn Squires, Chair	Steve Gallus
Joe Balyeat	Rick Laible
Vicki Cocchiarella	Dave Lewis
Mike Cooney	Jim Shockley
Jon Ellingson	Joe Tropila
Jeff Essmann	

SENATE – Business & Labor Committee

Vicki Cocchiarella, Chair	Carolyn Squires
Joe Balyeat	Donald Steinbeisser
Duane Grimes	Bill Tash
Dave Lewis	Jon Tester
Glenn Roush	Joe Tropila
Frank Smith	

Montana Lottery

September 2005

Montana Lottery Commission:

The Lottery will transfer \$1,526,239 to the General Fund as a result of operations in the fourth quarter of fiscal year 2005 compared to \$1,988,861 for the same time period last year. The total transfer for the year is \$6,222,555 or 86% of the budgeted transfer.

Powerball sales were down by more than \$3 million for this year compared to last year due to the absence of large jackpots in this year. In addition, Montana Cash and Wild Card sales were also lower while Hot Lotto experienced increased sales and scratch products remained stable. Qwik Tix were introduced in the third quarter of fiscal year 2004 with sales of \$243,552 compared to sales of \$436,301 in this year.

Direct game costs were consistent with sales for the quarter and the fiscal year. Net operating revenue as a percent of total revenue was 31% for fiscal 2005, compared to 33.0% for last year. Total operating expenses for the year of \$4,321,626 were slightly higher (4.9%) than last year's total of \$4,121,454 but still within our established budget.

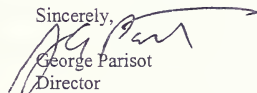
In late May, we introduced *Star Wars* to coincide with the movie release. It is performing well; after 15 weeks 65% of the game is sold out compared to another \$2 novelty game introduced a month earlier, which currently stands at 25% sold. We also introduced *Colossal Crossword*, our first \$5 crossword game. After 17 weeks, it has sold 35% and the other most recent \$5 game had sold only 26% for the same time period.

The Montana Lottery participated in Montana's two major fairs, Montana State Fair in Great Falls, and MontanaFair in Billings. Working with local Lottery retailers, Lottery staff sold and promoted Lottery products, and answered questions and shared information with customers from across the state. Other activities over the past few months included celebrating winners in retail locations such as Lewistown, Glasgow and Libby, among others. These events and activities are designed to increase public awareness about the Lottery and its winners.

The Powerball matrix change was accomplished August 28 as scheduled; however, at this time, it is too early to see what impact the change will have on jackpot growth and resulting sales.

The recent enhancements to the Powerball matrix, combined with a further emphasis on Scratch ticket sales and player outreach events such as fairs and winner events will position the Montana Lottery for future growth.

Sincerely,



George Parisot
Director



MONTANA LOTTERY
STATEMENT OF NET ASSETS
JUNE 30, 2005 and 2004
(UNAUDITED)

	Period Ended June 30, 2005	Period Ended June 30, 2004
ASSETS:		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 349,048	\$ 297,559
Receivables (Net)	1,349,901	1,149,380
Due from Primary Government	9	1,039
Due from Component Units	321	707
Inventories	1,100,853	1,034,181
Other Current Assets	<u>21,710</u>	<u>16,339</u>
TOTAL CURRENT ASSETS	2,821,842	2,499,205
NONCURRENT ASSETS		
Computer, Furniture & Equipment	5,563,895	5,563,836
Accumulated Depreciation	(4,819,838)	(3,929,838)
Software, net of Amortization	123,214	287,500
Multi-State Receivable	<u>1,326,136</u>	<u>1,325,275</u>
TOTAL NONCURRENT ASSETS	2,193,407	3,246,773
TOTAL ASSETS	\$ <u>5,015,249</u>	\$ <u>5,745,978</u>
LIABILITIES:		
CURRENT LIABILITIES		
Accounts Payable	\$ 525,788	\$ 474,326
Estimated Prize Liability	1,436,459	1,528,838
Due to Primary Government	7,918	209,763
Due to Component Units	5	279
Transfer Obligations	1,526,239	1,988,861
Deferred Revenue	100,634	63,777
Current Portion Comp. Absences	97,302	112,270
Other Current Liabilities	<u>0</u>	<u>6,000</u>
TOTAL CURRENT LIABILITIES	3,694,345	4,384,114
NONCURRENT LIABILITIES		
MUSL Prize Liability	1,257,803	1,283,395
Accrued Compensated Absences	<u>63,101</u>	<u>78,469</u>
TOTAL NONCURRENT LIABILITIES	1,320,904	1,361,864
TOTAL LIABILITIES	5,015,249	5,745,978
NET ASSETS		
Unrestricted Net Assets	<u>0</u>	<u>0</u>
TOTAL LIABILITIES AND NET ASSETS	\$ <u>5,015,249</u>	\$ <u>5,745,978</u>

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
FOR THE QUARTERS AND YEARS ENDED JUNE 30, 2005 and 2004
(Unaudited)

	Quarter Ended June 30, 2005	Quarter Ended June 30, 2004	Year Ended June 30, 2005	Year Ended June 30, 2004
OPERATING REVENUES:				
Scratch ticket revenue	\$ 2,724,628	\$ 2,546,294	\$ 10,535,046	\$ 10,378,002
Powerball revenue	3,771,358	3,781,034	13,886,091	16,972,086
Montana Cash revenue	1,129,676	1,074,020	3,830,187	4,186,863
Wild Card revenue	610,603	553,875	2,301,163	2,329,385
Hot Lotto/Rolldown revenue	801,968	658,479	2,820,996	2,435,021
Quik Tix revenue	95,678	192,749	437,762	436,301
License, permits, and misc	<u>24,273</u>	<u>1,088</u>	<u>30,023</u>	<u>2,543</u>
Total Operating Revenues	9,158,184	8,807,539	33,841,268	36,740,201
Less Direct Game Costs:				
Scratch ticket prize expense	(1,571,443)	(1,398,484)	(6,275,935)	(6,199,677)
On-line ticket prize expense	(3,239,469)	(3,065,099)	(11,527,966)	(12,480,211)
Retailer commission	(534,049)	(491,484)	(1,965,321)	(2,090,986)
Cost of tickets sold	(198,599)	(155,530)	(767,140)	(703,966)
Vendor fees	<u>(754,828)</u>	<u>(729,754)</u>	<u>(2,822,415)</u>	<u>(3,066,764)</u>
Net Operating Revenue	2,859,796	2,967,188	10,482,491	12,198,597
OPERATING EXPENSES:				
Advertising	301,078	132,400	606,394	634,098
Advertising Production	18,564	20,649	145,435	127,767
Audit Fees	3,577	4,670	22,333	43,335
Bad Debts Expense	20	(135)	3,187	1,829
Communications	23,769	25,147	91,550	89,905
Contractual Services	126,357	39,913	266,639	190,357
Depreciation and Amortization	267,640	267,116	1,069,531	1,064,432
Interest Expense	0	1,046	0	25,481
Administrative Service Fee	13,579	13,572	54,318	54,289
State Cost Recovery	3,317	2,458	13,270	10,558
Multi-State Dues	0	0	88,856	91,967
Public Relations	18,143	10,949	27,318	27,292
Other	16,250	10,237	35,814	26,383
Personal Services	369,300	346,060	1,455,722	1,400,905
Repairs and Maintenance	9,534	3,195	24,822	17,684
Supplies and Materials	151,111	79,115	273,592	192,914
Travel	11,514	6,011	31,778	13,538
Utilities and Rent	<u>28,208</u>	<u>27,635</u>	<u>111,067</u>	<u>108,720</u>
Total Operating Expense	1,362,021	990,038	4,321,626	4,121,454
Operating Income	1,497,775	1,977,150	6,160,865	8,077,143
NONOPERATING REVENUES (EXPENSES)				
Interest earnings	27,082	12,662	62,033	43,986
Gain/Loss on sale of asset	<u>1,382</u>	<u>(951)</u>	<u>(343)</u>	<u>(5,527)</u>
Total Nonoperating Revenues(Expenses)	28,464	11,711	61,690	38,459
Income Before Operating Transfers	1,526,239	1,988,861	6,222,555	8,115,602
Operating Transfers In (Out) - General Fund	<u>(1,526,239)</u>	<u>(1,988,861)</u>	<u>(6,222,555)</u>	<u>(8,115,602)</u>
CHANGE IN NET ASSETS	0	0	0	0
Total Net Assets, Beginning of Period	0	0	0	0
TOTAL NET ASSETS, END OF PERIOD	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN NET FUND ASSETS
AND RECONCILIATION OF BUDGET AND ACTUAL (BUDGETARY BASIS) TO GAAP BASIS
FOR THE YEAR ENDED JUNE 30, 2005
(Unaudited)

	<u>Budget</u> Fiscal Year July 1, 2004 - June 30, 2005	<u>Actual</u> Year Ended June 30, 2005 (Unaudited)	Actual as a Percent of Final Budget (%)
REVENUES:			
Scratch ticket revenue	\$ 10,300,000	\$ 10,535,046	102.28
Powerball revenue	17,000,000	13,886,091	81.68
Montana Cash revenue	4,200,000	3,830,187	91.19
Wild Card revenue	2,300,000	2,301,163	100.05
Hot Lotto revenue	2,350,000	2,820,996	120.04
Qwik Tix revenue	500,000	437,762	87.55
License, permits, and miscellaneous	2,000	30,023	1501.15
Total Revenues	<u>36,652,000</u>	<u>33,841,268</u>	92.33
DIRECT GAME COSTS:			
Prizes - Scratch ticket	6,077,000	6,275,935	103.27
Prizes - Lotto games	12,738,000	11,269,148	88.47
Prizes - Qwik Tix	310,000	258,818	83.49
Retailer commissions	2,156,500	1,965,321	91.13
Ticket cost - scratch games	721,000	767,140	106.40
Ticket cost - vendor fees	3,060,275	2,822,415	92.23
Total Direct Game Costs	<u>25,062,775</u>	<u>23,358,777</u>	93.20
OPERATING EXPENSES:			
Advertising	582,688	606,394	104.07
Advertising Production	203,770	145,435	71.37
Audit Fees	37,983	22,333	58.80
Communications	83,500	91,550	109.64
Contractual Services	366,713	266,639	72.71
Administrative Service Fee	54,318	54,318	100.00
State Cost Recovery	14,245	13,270	93.16
Multi-State Dues	115,502	88,856	76.93
Public Relations	35,950	27,318	75.99
Other	32,655	35,814	109.67
Personal Services	1,463,089	1,488,681	101.75
Repairs and Maintenance	25,402	24,822	97.72
Supplies and Materials	197,125	273,592	138.79
Travel	36,607	31,778	86.81
Utilities and Rent	112,242	111,067	98.95
Equipment	48,735	17,994	36.92
Total Operating Expenses	<u>3,410,524</u>	<u>3,299,861</u>	96.76
Operating Income	8,178,701	7,182,630	87.82
NONOPERATING REVENUES (EXPENSES):			
Interest Earnings	0	19,552	
Gain/(Loss) on Sale on Asset		(34.3)	
NET INCOME (BUDGETARY BASIS)	\$ 8,178,701	\$ 7,201,839	88.06
RECONCILIATION OF BUDGETARY/GAAP BASIS:			
1. Capitalized equipment purchases	48,735	17,994	36.92
2. Adjustment for compensated absences		32,959	
3. Adjustment for depreciation expense	(1,058,861)	(1,069,531)	100.06
4. Bad Debts		(3,187)	
5. MUSL interest earnings	50,000	42,484	84.96
Total Reconciling Items	(970,126)	(979,284)	
NET INCOME (GAAP BASIS)	\$ 7,208,575	\$ 6,222,555	86.32

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
ANALYSIS OF REVENUES AND EXPENSES BY PRODUCT
FOR THE YEAR ENDED JUNE 30, 2005
(UNAUDITED)

	SCRATCH	POWERBALL	MONTANA CASH	WILD CARD	HOT LOTTO	OWIK TIX	ADMIN
REVENUES:	\$ 10,535,046	\$ 13,886,091	\$ 3,830,187	\$ 2,301,183	\$ 2,820,996	\$ 437,762	\$ 30,023
DIRECT GAME COSTS:							
Prize Expense	6,275,935	6,551,240	2,144,720	1,210,114	1,363,074	258,818	0
Retailer Commissions	796,333	695,228	193,490	115,092	141,062	24,096	0
Cost of Tickets Sold	767,140	0	0	0	0	0	0
Vendor Fees	879,677	1,158,664	319,821	192,147	235,553	36,553	0
NET OPERATING REVENUE	1,815,961	5,480,959	1,172,156	763,810	1,081,287	118,295	30,023
OPERATING EXPENSES:							
Advertising	130,909	226,202	161,372	38,410	38,410	10,713	378
Advertising Production	21,025	46,100	26,057	19,516	19,515	12,971	251
Audit Fees	0	0	0	0	0	0	22,333
Bad Debts	0	0	0	0	0	0	3,187
Communications	54,004	459	459	459	459	459	35,251
Contractual Services	3,335	2,996	3,596	2,996	2,996	13,849	236,871
Depreciation and Amortization	302,949	452,240	125,434	75,401	92,198	15,018	6,291
Administrative Service Fee	18,377	5,591	4,142	2,705	2,686	2,695	18,122
State Cost Recovery	0	0	0	0	0	0	13,270
Multi-State Dues	0	11,428	0	25,087	11,679	0	40,662
Public Relations	3,787	2,728	2,728	2,728	2,728	2,728	9,891
Other	908	520	558	519	519	26	32,766
Personal Services	492,502	149,843	110,995	72,486	71,990	72,225	485,681
Repairs and Maintenance	0	0	0	0	0	0	24,822
Supplies and Materials	39,586	31,671	32,224	31,671	31,671	6,633	100,136
Travel	0	74	74	73	73	0	31,484
Utilities and Rent	0	0	0	0	0	0	111,067
TOTAL OPERATING EXPENSES	1,067,380	929,852	467,639	272,051	274,924	137,317	1,172,463
OPERATING INCOME	748,581	4,551,107	704,517	511,759	806,363	(19,022)	(1,142,440)
NONOPERATING REVENUES (EXPENSES)							
Interest Earnings	0	0	0	0	0	0	62,033
Gain(Loss) on Sale of Asset							(343)
TOTAL NONOPERATING REVENUES (EXPENSES)	0	0	0	0	0	0	61,690
NET INCOME BY PRODUCT	\$ 748,581	\$ 4,551,107	\$ 704,517	\$ 511,759	\$ 806,363	(19,022)	(1,080,750)
PROFIT AS A % OF REVENUE	7.11%	32.77%	18.39%	22.24%	28.58%	-4.35%	N/A

NOTE: THIS IS ONLY ONE YEAR'S ACTIVITY AND THEREFORE SHOULD NOT BE INTERPRETED TO SHOW HOW OUR PRODUCTS HAVE PERFORMED IN PAST YEARS OR WILL PERFORM IN THE FUTURE.

MONTANA LOTTERY
Notes to the Financial Statements (Unaudited)
June 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity.

The Montana Lottery, established under the provisions of Section 23-7-101, Montana Code Annotated (MCA), was approved by the Montana electorate through Legislative Referendum No. 100 on November 4, 1986.

Montana's first lottery tickets went on sale June 24, 1987.

The Montana Lottery is operated by a five-member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the types and forms of lottery games, set the ticket price, number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games in conjunction with other lottery states and countries, and prepare financial reports. The Montana Lottery is attached to the Montana Department of Administration for administrative purposes.

The Montana Lottery is included as an enterprise fund in the State of Montana's Comprehensive Annual Financial Report. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Montana Lottery's financial statements as a reporting agency.

Basis of Presentation. The Montana Lottery reports its financial activity in accordance with generally accepted accounting principles (GAAP) as prescribed in pronouncements of the Governmental Accounting Standards Board (GASB).

Enterprise Fund. The Montana Lottery is classified as an Enterprise Fund of the Governmental Proprietary Fund Type. Enterprise Funds account for operations: a) financed and operated similar to private business enterprises, where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or b) where the Legislature has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate.

Basis of Accounting. The Montana Lottery's financial statements are prepared using the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

Revenue Recognition. Lottery scratch ticket sales are recorded as revenue based on the time the retailer activates the pack of tickets for sale. In accordance with an established policy, retailers may return unsold tickets to the Lottery for credit. Sales are decreased by an allowance for estimated ticket returns.

Ticket sales for lotto games, Powerball, Wild Card, Montana Cash, and Hot Lotto are recorded as revenue based on drawings. Tickets sold in advance for future drawings are recorded as deferred revenue until such time as the tickets become valid for the most current drawing. Qwik Tix revenue is recognized at the time of sale by the retailers.

Free Tickets. Some Montana Lottery scratch games award free tickets as prizes. Net lottery ticket revenue does not include the value of free tickets given away and free plays won. The face value of these free ticket prizes distributed for the quarter and fiscal year ended June 30, 2005 was zero.

Promotional Credits. The Lottery issues promotional credits to retailers to be used to distribute free tickets to players. The tickets are distributed as part of a promotion run by the retailer, e.g., "Ask for the Sale" or second chance drawings. The Lottery also directly distributes scratch tickets for promotional purposes at trade shows, for media give-aways, and during new game introductions. The tickets distributed as a result of promotional credits are reflected as a reduction in revenue. The related prize expense and ticket cost for all promotions are reclassified as an advertising expense. For the quarter ended June 30, 2005, promotional credits resulted in a revenue reduction of approximately \$63,107 and an advertising expense reclassification of approximately \$38,036. For the fiscal year ended June 30, 2005, promotional credits resulted in a revenue reduction of approximately \$109,835 and a prize expense reclassification of approximately \$71,629.

Prizes. Expenses for scratch prizes are recorded based on the predetermined prize structure for each game. Expenses for lotto and Qwik Tix prizes are recorded based on the predetermined prize structure for each individual game. No prize expense is recorded for free tickets distributed.

Unclaimed Prizes. Prizes for the lotto games must be claimed within six months after the appropriate draw date. Prizes for scratch games must be claimed within six months of the announced end of each game. Qwik Tix prizes must be claimed within six months of the sale date. The unclaimed prize amounts are taken as a reduction in the Lottery Prizes Payable liability and the Prize Expense and are transferred to the State of Montana General Fund as a portion of the quarterly transfer. The amount of unclaimed prizes for all games is represented in the table below.

	Quarter Ended 6/30/05	Quarter Ended 6/30/04	Year To Date 6/30/05	Year To Date 6/30/04
Lotto & Qwik Tix	\$140,996	\$160,278	\$534,630	\$1,063,705
Scratch	<u>128,462</u>	<u>176,837</u>	<u>251,551</u>	<u>232,349</u>
TOTALS	\$269,458	\$337,115	\$786,181	\$1,296,054

2. SUMMARY OF ACCOUNTS

Cash and Cash Equivalents. Cash and cash equivalents consist of interest-bearing deposits with the Montana Board of Investments short-term investment pool, cash on deposit with a bank and cash on deposit with the Montana State Treasurer that is part of the State's pooled cash and is not separately identifiable as to specific types of securities. These funds are highly liquid and may be drawn on daily.

Cash and cash equivalents consist of the following:

	June 30,	
	2005	2004
Short-term investment pool	\$186,928	\$1,766
Cash on deposit with State Treasurer	151,970	285,643
Cash in revolving deposit account	10,000	10,000
Petty Cash	150	150
TOTALS	\$349,048	\$297,559

Reference to the State of Montana's Comprehensive Annual Financial Report would identify the level of risk associated with cash and cash equivalents in the short-term investment pool and amounts retained with the State Treasurer. The bank balance of the revolving deposit account was \$54,676 at June 30, 2005 and was covered by federal depository insurance. The carrying amount reported in the balance sheet for cash and cash equivalents approximates the fair market value.

Receivables. Receivables include \$1,435,269, representing amounts due the Lottery for tickets purchased by retailers. An allowance for doubtful accounts is reported as net of receivables and is based on historical perspective. As of June 30, 2005 the allowance is zero. An allowance for ticket returns is also included in the receivables amount. This allowance represents a reduction in receivables at

June 30, 2005, for estimated ticket returns. This is an estimate based on returns received to date, as well as, an estimate of tickets unsold by retailers for games that have a public sale end date prior to July 1, 2005. The allowance for ticket returns is \$93,089 at June 30, 2005. The return of vendor fees related to the allowance for returns is \$7,721.

Inventories. Inventories consist of merchandise and supplies inventories. Merchandise inventory includes scratch tickets valued at \$969,756 stored in the warehouse, at retailers prior to being activated by the retailer and with the marketing representatives. These ticket inventories are recorded at cost using the specific identification method and maintained on a perpetual inventory system. Tickets are charged to cost of tickets sold upon activation or after game end.

Supplies inventories include ticket dispensers, premiums and point-of-sale materials. At quarter end, supplies inventories totaled \$131,097. These inventories are also recorded at cost using the specific identification method.

Other Current Assets. Other current assets consist of the following:

	June 30,	
	2005	2004
Prepaid Expenses	19,960	11,539
Employee Advances	<u>1,750</u>	<u>4,800</u>
TOTALS	\$21,710	\$16,339

Transfer Obligations. The account "Transfer Obligations" is \$1,526,239 payable to the General Fund at June 30, 2005.

Compensated Absences. State employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Vacation leave may be accumulated not to exceed two times the maximum number of days earned annually. With no limit on accumulation, sick leave is earned at 12 days per year. Upon retirement or termination, an employee is paid 100% for unused vacation and 25% for unused sick leave. The Lottery's liability for compensated absences is detailed below.

Balance	Net Leave	Balance
<u>June 30, 2004</u>	<u>Earned/(Used)</u>	<u>June 30, 2005</u>
\$190,739	(\$30,336)	\$160,403

Commissions. Section 23-7-301(10), MCA, provides retailers a commission on scratch, Qwik Tix and lotto tickets or chances sold. The Lottery Commission established this commission at 5% of the face value of scratch tickets activated by the retailers and the face value of Qwik Tix and lotto tickets sold. In addition

retailers can earn bonus commissions on tickets sold based on incremental sales of scratch tickets and Qwik Tix. During the quarter and fiscal year ended June 30, 2005 retailers earned bonus commissions of \$74,139 and \$268,844 respectively. For the quarter and fiscal year ended June 30, 2005 total commissions were \$534,049 and \$1,965,321 respectively.

3. **MARKETING PRODUCTION EXPENSES**

The Lottery has contracted with several vendors to provide marketing related services and materials. These services include media placement, creative design and layout, and media production. Those services and materials not included in the Advertising and Advertising Production expense categories are printing and ticket dispensers. The cost of these services and materials, included in Operating Expenses as Contracted Services and Supplies and Materials, are detailed below for the fiscal year ended June 30, 2005:

Printing	\$21,854
Customer Display Units (CDU)	7,456
"Play Here" signs	102,225
Ticket Dispensers	<u>24,255</u>
	\$155,790

4. **PAYMENTS TO OTHER STATE AGENCIES**

The Lottery receives a variety of services and supplies and materials from other state agencies. These services and materials are detailed below for the fiscal year ended June 30, 2005:

Insurance	\$ 24,250
Warrant Writing Services	541
Payroll Services	1,037
Audit Fees	2,333
Work Study Contracts	36
Computer Fees	25,311
Printing	1,781
State Accounting System Support	9,010
Supplies and Materials	3,584
Mail Processing Fees	5,035
Telecommunications	18,395
Public Relations	7,000
Administrative Service Fees	54,318
SWCAP and SFCAP	10,884
Other	<u>5,268</u>
TOTAL	\$168,783

5. PRIZES

Paid Prizes. Section 23-7-402, MCA states, "A minimum of 45% of the money paid for tickets or chances must be paid as prize money". Prize expense is recorded based on the predetermined prize structure percentage for each game less unclaimed prizes. For the quarter ended June 30, 2005, the prize expense of \$4,810,912 is 52.67% of net Lottery ticket revenue of \$9,133,911. For the fiscal year ended June 30, 2005, the prize expense of \$17,803,901 is 52.66% of net Lottery ticket revenue of \$33,811,245.

6. TRANSFER TO STATE GENERAL FUND

Section 23-7-402(3), MCA, states "That part of all gross revenue not used for payment of prizes, commissions, and operating expenses, together with the interest earned on the gross revenue while the gross revenue is in the enterprise fund, is net revenue. Net revenue must be transferred quarterly from the enterprise fund established by 23-7-401 to the State General Fund." For the quarter ended June 30, 2005, the net revenue payable to the State General Fund totaled \$1,526,239.

7. MULTI-STATE LOTTERY JOINT VENTURE

In November 1989 the Montana State Lottery joined the Multi-State Lottery Association (MUSL). MUSL was created in September 1987 to operate a multi-state lottery game for the benefit of party lotteries. Powerball, Wild Card, and Hot Lotto are the games jointly operated by the members, in which Montana presently participates. Each lottery participating in MUSL is represented on the Board of Directors.

The Multi-State Lottery Receivable with a balance of \$1,326,136, as of June 30, 2005 is comprised of several reserve accounts, which are maintained by the Multi-State Lottery Association (MUSL). The balance of these reserve accounts is as follows:

Powerball Prize Reserve Account	\$600,561
Powerball Unreserved Account	68,333
Powerball Set Prize Reserve Account	177,500
Wild Card Reserve Account	415,074
Hot Lotto Set Prize Reserve Account	<u>64,668</u>
TOTAL	\$1,326,136

The Powerball Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Powerball game, assuming that no unanticipated prize claims have been paid. Interest earned on the Lottery's share of the fund, represented by the Unreserved Account, would be returned to the Lottery upon leaving MUSL. The amounts in the Unreserved Account may be used at the Board's discretion.

The Powerball Set Prize Reserve Account is used to fund prize payments for current drawings. Since the Powerball game has fixed prizes, it is often necessary to draw from this reserve to fund payment of prizes at the fixed amount. This account would be returned to the Lottery upon withdrawal from the Powerball Game.

The Lottery contributes to these reserve funds through the 50% set aside for prizes. In addition the Lottery was required to contribute for its portion of the reserve funds accumulated since the start of the Powerball game. The Lottery made this payment in full as of June 1990, through an additional 2% of drawing revenue rather than making a lump sum payment. Payments made to this fund are considered a portion of prize expense associated with the game.

The Wild Card Reserve Account is to be used in the event of an unanticipated prize claim on the Wild Card game. This account is also administered by MUSL and would be returned to the Lottery one year after the Wild Card Product Group of Idaho, Montana, South Dakota, and North Dakota is disbanded. The Lottery contributes to this account through the 55% set aside for prizes. Payments made to this fund are considered a portion of prize expense related to the Wild Card game.

The Hot Lotto Set Prize Reserve Account is administered by MUSL and is to be used only in the event of unanticipated prize claims. Like other MUSL games the reserve amount would be returned to the Lottery one year after withdrawal from the Hot Lotto game. The Lottery contributes to the reserve through the 50% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game.

8. GAMES

Currently, the Montana Lottery games are scratch ticket games, four lotto games referred to as Powerball, Montana Ca\$h, Wild Card, and Hot Lotto and four instant play/instant win games referred to as Qwik Tix.

Scratch ticket games provide players the opportunity to win instantly by scratching a latex covering to reveal a prize.

The Powerball game allows players the chance to win a minimum pari-mutuel jackpot of approximately \$10 million. A player must match all 6 numbers to win the jackpot; players win prizes ranging from \$3 to \$100,000 for matching less than all 6 numbers. Drawings are held twice weekly on Wednesday and Saturday nights. For any drawing, if no ticket matches 6 out of 6 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot. In March 2001, the Lottery added Power Play to the Powerball game. For an additional bet, the Power Play option provides non-jackpot winners the chance to multiply their prize amount by a factor of two through five.

The Montana Ca\$h game allows players the chance to win a minimum pari-mutuel jackpot of \$20,000. Players select 5 numbers from a field of 37 and must match at least 3 out of 5 to win a prize. Matching 3 of 5 wins \$5 and 4 of 5 wins \$200. The drawing is conducted twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot.

The Wild Card game allows players the chance to win a pari-mutuel jackpot, with a guaranteed minimum of \$100,000. Players select 5 numbers from a field of 31 plus one of 16 face cards and must match all 5 numbers and the wild card to win the jackpot; players win prizes from \$1 to \$5,000 for matching less than all 5 numbers and/or the wild card. Drawings are held twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers and the wild card, the jackpot rolls over to the next drawing to create a progressive jackpot.

Hot Lotto allows players the chance to win a pari-mutuel jackpot with a guaranteed minimum of \$1 million. Players choose 5 numbers from a field of 39 plus 1 Hot Ball number from a field of 19; the first 5 numbers and the Hot Ball must be matched to win the jackpot. Players can win prizes ranging from \$2 to \$10,000 by matching less than all 5 numbers and/or the Hot Ball. If no ticket wins the jackpot, it rolls over to the next drawing to create a progressive jackpot. Drawings are held twice weekly on Wednesday and Saturday nights.

Qwik Tix is a product line introduced by the Lottery in February 2004. There are four games, each with its own play style and prize structure. The four games are Lucky Numbers, a number match game; Hot Tac Toe, a tic tac toe grid; Jacks or Better, a poker game; and Montana Match, a match three symbols game. The Qwik Tix tickets are printed at the lotto terminal at the time of sale and can be redeemed immediately, with the maximum prize being \$500. Each ticket costs \$2 and consists of either two plays of a single Qwik Tix game or one play of a Qwik Tix game and one play of a related lotto game. The lotto games sold in this manner are exactly

the same as lotto tickets sold separately and cannot be redeemed until the appropriate drawing.

9. COMMITMENTS - GAMING SUPPLIER CONTRACTS

Scratch Tickets. On June 27, 2001 the Montana Lottery Commission approved the award of a one-year contract with Oberthur Gaming Technologies Corp. (Oberthur) for the provision of scratch tickets; the resulting contract was signed on August 8, 2001. The contract is for one year with the option for six additional one-year renewals. The contract contains specifications regarding ticket design, printing, game ownership, inspection, and prize structure.

Oberthur, as the vendor, provided a performance bond covering the contract term and an errors and omissions policy covering an ultimate net loss of \$7,500,000. The Lottery may terminate this contract by providing proper notification to Oberthur.

On-line Services. On August 18, 1998, the Lottery signed a seven-year contract with Autotote Lottery Corporation to provide an on-line gaming system and associated services beginning March 28, 1999. The contract provides for payments to be made for the purchase of an on-line gaming system including terminals and software. The Lottery paid Autotote Lottery Corporation \$5,025,311 for the system on April 26, 1999. Payment under the contract is also based on 8.35% of weekly Lottery sales.

10. CONTINGENT LIABILITIES - PRIZE ANNUITIES

During fiscal year 1989, the Montana Lottery awarded four Big Spin Jackpot prizes totaling \$5,000,000. The Lottery made the initial payments to the winners in the amount of \$253,088 and on September 26, 1988 the Montana Lottery awarded annuities in the amount of \$2,350,180 to Western National Life. Through these annuities, Western National Life makes the remaining payments to the Big Spin Jackpot winners. As of June 30, 2005 the contingent liability for future prize payments funded through the purchase of annuities was \$465,000.

11. LOTTO*AMERICA/POWERBALL/TRI-WEST JACKPOT PRIZES

Jackpot prizes awarded in the Lotto*America/POWERBALL and TRI-WEST LOTTO games are funded through the purchase of U.S. Treasury Zero-Coupon Bonds purchased in the name of the Montana Lottery by MUSL. MUSL will cash the bonds

each year as they mature and will wire the funds to the Lottery for payment to winners on the Anniversary date of the win.

On January 13, 1990 the Montana Lottery awarded its first Lotto*America jackpot prize totaling \$1,740,000. The first annual payment of \$87,000 was made on February 1, 1990. On May 9, 1990 the Lottery awarded a second Lotto*America jackpot prize of \$3,000,000. The first annual payment of \$150,000 was made on May 23, 1990. A third jackpot prize was awarded on February 2, 1991 for \$7,360,000. The first annual payment of \$368,000 was made February 15, 1991. On November 23, 1991 a fourth jackpot prize was awarded totaling \$46,967,738.57. The first annual payment of \$2,355,738.57 was made December 12, 1991. On April 11, 1992 a fifth jackpot prize was won totaling \$2,000,000. The first annual payment of \$100,000 was made on April 27, 1992.

On July 6, 1994 the Montana Lottery awarded its first Tri-West Lotto jackpot prize totaling \$700,565. The first annual payment of \$35,000 was made on July 26, 1994.

On July 22, 1995 the Montana Lottery awarded its first Powerball jackpot prize totaling \$31,401,655.99. The first payment of \$1,571,655.99 was made on August 8, 1995. On April 5, 1997 the Lottery awarded a second Powerball jackpot prize totaling \$11,000,000. The first annual payment of \$550,000 was awarded on April 18, 1997.

As of June 30, 2005 the combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Lotto*America winners was \$17,476,739. The combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Powerball and Tri-West Lotto winners was \$22,065,210.

On March 27, 1999 the Montana Lottery had a Powerball jackpot winner. The prize was \$35.1 million (\$19.35 million cash option). The winner chose the cash option and was paid a lump sum in June 1999.

12. LEASES

Rent. The Montana Lottery leases its office, administrative and warehouse facilities under a noncancelable lease agreement that is effective March 2002 through February 2007. The monthly lease payments through February 2006 are \$7,476 and will increase 1.5% per year.

13. LONG-TERM DEBT

Note Payable. A contract with Autotote Lottery Corporation required the purchase of an online gaming system including terminals and software. The Lottery paid Autotote Lottery Corporation \$5,025,311 for the system by entering into a loan agreement with Norwest Investment Service, now known as Wells Fargo Brokerage Services, LLC. The loan will be repaid in quarterly installments of \$286,394.30 over five years. The first payment was due July 26, 1999. The interest rate on the loan is 5.12%. The loan was paid in full in April, 2004.

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